STATEMENT OF FRANK A. SUELLENTROP

SUBCOMMITTE ON FINANCIAL INSTITUTIONS AND CONSUMER PROTECTION

UNITED STATES SENATE

Chairman Brown, Ranking Member Corker and Members of the Subcommittee: thank you for the opportunity to testify before you today regarding the topic of "Enhancing Safety and Soundness: Lessons Learned and Opportunities for Continued Improvement."

My name is Frank Suellentrop and I am President and Chairman of Legacy Bank in Colwich, Kansas. We are a $250 million closely-held community bank providing banking services to the area of Sedgwick County, Kansas. We have five branch locations: our charter bank location in Colwich, Kansas, population 1,400, and four branch locations in the Wichita, Kansas community.

Our bank was established in February 1886, which means that we are celebrating 125 years in 2011. I am fourth generation President of our bank with over 38 years of employment at Legacy Bank. I have been President of our bank since 1991. From that experience, I have seen the beginnings of consumer regulation in the early 1970's, the agriculture crisis, the savings & loan and real estate crisis of the 1980's and early 1990's. and now, the Wall Street-induced real estate crisis of 2008.

Legacy Bank is significantly involved in residential development, residential construction, and commercial property lending and therefore, has been impacted greatly by the economic slowdown and depressed real estate market values. Fortunately, the economy in the Wichita, Kansas area has fared reasonably well throughout the current crisis relative to other markets, primarily due to the fact that Kansas, specifically Wichita, had not experienced inflated real estate values of the past decade.

I would like to preface my comments regarding a recent examination by saying that I understand examiners are charged with a difficult task. On one hand, they are expected to protect against bank failures, insure consumer compliance and regulation are adhered to, satisfy community groups and organizations demand for fair banking practices, and Congressional demands for banking/financial oversight. On the other hand, regulators are/should be tasked with not interfering with a bank's corporate mission of creating value for its shareholders. Legacy Bank is a "for-profit" corporation. Our most recent 2010 examination revealed stark differences from prior exams: higher capital and liquidity standards, more demanding asset quality evaluations, expectations for higher allowance for loan & lease loss reserves ("ALLL"), and increased focus on management assessment and compensation practices.

Comments made by regulators during our last exam include, "We don't like your risk profile" and "We're not going 'to bat' for you in Washington." To put the first comment in context, our bank has been a lender to residential real estate developers, homebuilders, and commercial property owners since the late 1980's. We feel our lending staff has the experience and knowledge to manage our loan portfolio composition. These comments were significantly more aggressive compared to prior examination observations. Due to recent failures or problem banks in other areas of the country, our lending 'risk profile' is now unacceptable. In addition to standard loan underwriting criteria of evaluating a borrower's capital, collateral, capacity to repay, and market conditions, we have added a new component to our loan approval discussion process – "Will the loan pass examiners' review and approval?" This component should not be a loan approval consideration. A customer's loan request should be based on its viability and productive value. With respect to the latter comment, it illustrates a regulatory attitude that all banks in real estate lending are unsafe and unsound in their practices.

Banks are evaluated based on their CAMELS component ratings, which measures a bank's capital, asset quality, management, earnings, liquidity and sensitivity to interest rates. My comments on each of these bank evaluation components under the current regulatory environment are provided below.

Capital

Capital standards for most banks are being dictated above levels for regulatory defined 'well-capitalized' banks and standards required for our nation's largest financial institutions. Regulators are using their discretionary capital standards caveat to demand capital levels above those banks defined as 'well-capitalized'. Capital below the mandated Tier-One and risk-based levels are likely to receive a lower 'capital component,' which may subject banks to a 'troubled bank' status. Discretionary capital standards create a difficult moving target for banks as we seek to achieve an acceptable capital component rating.

Asset Quality

Examiners are slow to recognize when credit risk has been mitigated. Classifications are inconsistent. No credit given for past performance of the borrower. Some classifications are backdated after the borrower begins to show improvement.

Management

Management compensation is now being reviewed by examiners, suggesting potential negative impact to earnings and capital. Without significant discussion during our last examination, examiner comments dictated a requirement that we justify management compensation and benefits. Somehow 'Wall Street' excesses on executive pay have crept into regulators view of 'Main Street' banking compensation practices when there is no valid comparison to their abuses.

Earnings

Earnings evaluations are focused on budget expectations and provide a source of capital growth. Budgets are a fluid document where changes occur relative to changing market conditions. Variances occur throughout the year and are detailed in monthly review of performance vs. a re-budgeting process as suggested by an examiner.

Liquidity

Current examination expectations dictate a higher level of liquidity to protect against the "what ifs" for funding assets. Examiners are reluctant to recognize the value of purchased funding costs vs. core deposit funding. Levels of purchased funding should be variable to the institution and not an industry standard.

At each examination, an Examiner in Charge ("EIC") is designated. My experience with this practice is that often an EIC does not want to overrule another examiner's findings regarding loan quality issues or other components of an examination. On completion of an examination, EIC comments are submitted to a Review Examiner. The Review Examiner then does not want to overrule an EIC's submitted comments; therefore, the process can be problematic for bankers where an inexperienced or unqualified examiner's findings become a part of the 'report of examination.' These results then become a part of the final report for bank examination ratings and mandated actions to address findings. Only experienced examiners capable of managing others' activities should be designated as an "Examiner in Charge" to insure quality in a final report of examination. Recourse for bankers disputes regarding examination findings are often treated as we agree to disagree by examiners.

In summary, micro-managing is unproductive. Part of the regulator's role is to offer insight into latest industry trends and issues. Instead, exam outcomes now seem predetermined with enforcement actions imposed for minor issues that do not enhance a bank's viability. To move forward in a productive, mutually beneficial manner, there should be more focus on the root cause of examination findings. Examiners should expect results, but if capital is solid and management is capable, then over-regulation is unnecessary. Regulatory burden and examiner expectations are disproportionate in their impact on community banks vs. the largest banks. Many community banks have a limited staff to respond to examiner expectations vs. the largest banks full time staff devoted to regulatory compliance.

Thank you again for the opportunity to comment. I hope that this testimony provides productive insight into the current regulatory environment for community banks.